* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Reserved on: 6th September, 2012
Date of Decision: 20th November, 2012

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\+ **ITA 417/2003**
\+ **ITA 18/2004**
\+ **ITA 722/2007**
\+ **ITA 770/2011**
\+ **ITA 1050/2011**
\+ **ITA 1051/2011**

COMMISSIONER OF INCOME TAX .....Appellant
Through: Mr. Abhishek Maratha, Sr. Standing Counsel with Ms. Anshul Sharma, Advocate.
Mr. Kamal Sawhney, Sr. Standing Counsel.

Versus

MEHTA CHARITABLE PRAJNALAY TRUST .....Respondent
Through: Mr. Ajay Vohra with Ms. Kavita Jha and Mr. Somnath Shukla, Advocates.

CORAM:
MR. JUSTICE S. RAVINDRA BHAT
MR. JUSTICE R.V. EASWAR

R.V. EASWAR, J.:

For detailed order see ITA No.309/2003.

(R.V. EASWAR)
JUDGE

(S. RAVINDRA BHAT)
JUDGE

NOVEMBER 20, 2012
hs/vld

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These are seven appeals filed by the Revenue under Section 260A of the Income Tax Act, 1961 ('Act', for short). The relevant assessment years are 1992-93 to 1994-95, 2001-02 and 2005-06 to 2007-08. In all the appeals except the appeal in ITA No.722/2007, the following substantial questions of law have been framed: -

> "*(a) Whether the Tribunal was correct in law in confirming the order of CIT (A) and thereby holding that the assessee is entitled to exemption under Section 11 of the Income Tax Act?*

(b) Whether the Tribunal was justified in law in relying on its earlier order for A.Y. 1992-93 and thereby holding that the business activities carried on by the assessee were incidental to the main aims and objects of the Trust which are of Charitable nature?"

2. In respect of ITA No.722/2007 only question No.(a) has been framed.

3. The respondent – assessee in all these appeals is the Mehta Charitable Prajanalay Trust. It was created by a trust deed drawn up on 08.09.1971 by B. D. Mehta, partner of the firm M/s. Bishan Das Girdharilal and Raj Kumar Mehta, S/o. B. D. Mehta, partner of M/s. Raj Kumar & Sons Co. These are the two founder – trustees. They settled an amount of ₹2,200/- upon trust. Admittedly, this is the only property settled on the trust. The trust deed set out the objects of the trust which included the establishing and maintaining of schools, colleges and study circles, advancing education and research study on the modern and ancient Indian thought, providing for mental, moral and spiritual development, imparting real education, laying the foundations of high class character, inculcating the spirit of nationalism and patriotism, arranging for interpretation of ancient Hindu literature, preparing and publishing text books, providing food, clothing, shelter and medicines to needy persons, running of medical dispensaries, hospitals, etc. Clause 19 of the trust deed provided that the trust may "*carry on any business for and on behalf or in the name of the trust for the sole object of applying the income and profits thereof for the purposes of objects of the trust*". Another fact to be noticed here is that the founder – trustees were partner of firms which were themselves engaged in the business of the manufacture and sale of *Katha*.

4. After the formation of the trust, a business was commenced in the name of the trust for the manufacture of *Katha*. The funds for this business admittedly came from sister concerns of the firms in which the founder – trustees were partners and borrowings from banks and other agencies. A production unit was set up in the name "Mahesh Udyog" at Mahesh Nagar in District Una, Himachal Pradesh in the year 1972. This unit started production on 08.02.1973. Sometime

in the year 1978, this unit was leased to M/s. Shankar Trading Co. (P) Ltd., a sister concern in which close relations of the trustees held substantial interest. The unit continued to be run by the aforesaid company. The trust was in receipt of monthly lease rental since then; the rental was revised sometime in the years 1989 and 1991. The trust makes purchases and sale of *Katha* and *cutch* in its head office mainly through the two concerns in which the founder trustees had substantial interest.

5. We are not aware what happened prior to the assessment year 1989-90. However, for the said assessment year, the assessee seems to have claimed exemption under Section 11 in respect of its income and filed a return of income on that basis. The exemption was denied and on appeal to the CIT (Appeals), it was held that the business in *Katha* was carried on by the trustees or the Board of Directors and not by the beneficiaries of the trust and therefore in view of clause (b) of Section 11(4A) as it existed at that time, it was held that the trust was not entitled to the benefit of exemption. Thus the assessment was upheld by the CIT (Appeals). It is not known whether there was any further appeal to the Tribunal. In respect of the assessment year 1990-91, a similar view was taken by the assessing officer in the assessment proceedings. On appeal the CIT (Appeals) noted that the assessee was registered as a charitable trust and its activities did not involve any commercial activity for the purpose of making profits; it was held that the case fell under Section 11(4A) (b) of the Act and to this extent the benefit of the exemption was not available. To this extent his view was the same as the view of his predecessor for the assessment year 1989-90. However, he proceeded to examine the case in the light of the judgment of the Madras High Court in the case of *Thanthi Trust v. CBDT*, (1995) 213 ITR 639 and held that the business was held under trust and therefore the provisions of Section 11(4) applied to the exclusion of Section 11(4A) of the Act. In short, he held that it was a case of property (i.e. the business undertaking) being held under trust in accordance with Section 11(4) of the Act. He accordingly directed the assessing officer to allow the exemption.

6. In respect of the assessment year 1992-93, which is the first assessment year with which we are concerned in the present batch of appeals, the assessee filed its income tax return on the same basis claiming exemption under Section 11 of the Act. In the assessment made under Section 143(3) of the Act, the assessing officer held, following his predecessor's view, that the business was carried on not by the assessee – trust, but by the Board of Directors of the company who are managing the business. He, therefore, held that the provisions of Section 11(4) of the Act were not applicable and the provisions of Section 11(4A) of the Act were applicable. He noted that in the Delhi office the trading activities comprised of purchases and sales made through sister concerns in which the founder trustees were substantially interested and the claim of the assessee that the work in connection with the business of the trust is mainly carried on by the trustees was not supported by the facts. He also observed that the affairs of the trust were closely controlled by the two founder – trustees and the beneficiaries i.e. the members of the public did not have any say. He further held that the profits and gains of the business were not incidental to the attainment of the objects of the trust. In this view of the matter the benefit of Section 11 of the Act was denied and the assessment was completed on a total income of ₹62,86,390/- consisting of the profits of the *Katha* business.

7. In the appeal filed against the assessment, the assessee contended that it was a public charitable trust existing for the benefit of the members of the public, that it was registered with the CIT under Section 12A, that the business was carried on by the beneficiaries of the trust in furtherance of the objects, that the provisions of Section 11(4) of the Act and not Section 11(4A) were applicable, that the business of the trust was not carried on with the motive of earning profit but only with a view to deriving, income for running the charitable hospitals, dispensaries, schools, etc. and that if the primary purpose of the trust was charitable and if the other activities are not driven by profit motive, exemption under Section 11 of the Act could not be denied. These submissions were sought to be supported by the judgment of the Supreme Court in the case of *Addl. CIT v. Surat Art Silk Cloth*

Manufacturers, (1980) 121 ITR 1. It was further urged that the amendment to sub-section (4A) of Section 11 w. e. f. assessment year 1992-93 made the provisions more liberal and that having regard to the judgment of the Madras High Court in *Thanthi Trust* (supra) the assessee should be granted exemption under Section 11. The CIT (Appeals) was not persuaded by the submissions of the assessee. After examining the trust deed, he made a distinction between the objects of the trust and the powers of the trustees and held that though the objects as per the trust deed were undoubtedly charitable, clauses 19 and 20 which permitted the trust to carry on any business and to borrow monies from banks, individuals, financial institutions and business houses are not really the objects, but were clauses stipulating the powers of the trustees. Having thus made a distinction between the objects and powers, the CIT (Appeals) proceeded to examine Section 11(4A) vis-à-vis Section 11(4) of the Act. He held that the amended provisions of Section 11(4A) would apply from the assessment year 1992-93 onwards, and the effect of the amendment was that the benefit of exemption under Section 11 of the Act was not available to the income arising from profits and gains of business unless the business is incidental to the attainment of the objects of the trust and separate books of accounts are maintained by the trust in respect of the business. He held that there was no dispute that separate accounts were maintained in regard to the business. With regard to the main contention of the assessee that the Section 11(4A) of the Act did not have any application to the assessee's case because the business itself was held under trust, the CIT (Appeals) was unable to agree with the assessee. According to him the facts in *Thanthi Trust* (supra) were different; there, the founder of the trust was carrying on the business of printing and publishing a Tamil daily newspaper as its sole proprietor and the business itself was settled upon trust. In the present case, according to the CIT (Appeals), the trust was formed with a cash of ₹2,200/- contributed by the two founder trustees but no business undertaking as such was settled upon trust. On the basis of this distinction, the CIT (Appeals) took the view that the judgment of the Madras High Court did not apply.

8. The aforesaid view of the CIT (Appeals) was sufficient to dispose of the appeal before him but for the sake of completeness and in deference to the arguments taken before him, he proceeded to consider the case on the assumption that the judgment of the Madras High Court applied to the assessee's case. He observed that even if the judgment is held applicable to the present case, the question to be examined would be whether the business can be considered to be property held under the trust or is only a business carried on by or on behalf of the trust by virtue of the powers conferred upon the trustees under clauses 19 and 20 of the trust deed. The other question, according to the CIT (Appeals), that would arise for consideration was whether the business so carried on is incidental to the attainment of the objects of the trust as stipulated in the amended Section 11(4A) of the Act.

9. So far as the first question is concerned i.e. whether the business itself was held under trust, the CIT (Appeals) held that where the trustees decide to carry on the business in the name of the trust by borrowing funds or diverting money from sister concerns, it cannot be a case of property being held under trust but would be only a case of business being carried on for and on behalf of the trust. He made a distinction between borrowings made for the purpose of facilitating the running of business held under trust and borrowings made for the purpose of carrying on a business for and on behalf of the trust, where such borrowings constituted the basic source for the commencement of the business. According to the CIT (Appeals), if this distinction is not maintained, there can be no case where the business would not be property held under trust or where the business can be said to be carried on for and on behalf of the trust in contrast to the business itself being held under trust. He noted that after the trust was created, the sister concerns in which the founder – trustees or their close relatives had substantial interest diverted funds in favour of the business and some borrowings were also made from the banks and the business was started. Within a year a manufacturing unit of *Katha* and *cutch* was set up and became functional; the business started earning profits and they were utilised to pay off the debts. In 1978 the unit was leased to M/s. Shankar

Trading Co., a sister concern which had also contributed initially for the business and in which the trustees and their close relatives had substantial interest. The lease rent initially fixed was ₹25,000/- per month which was revised to ₹50,000/- per month from 01.04.1987 and to ₹1,00,000/- per month from 31.12.1991.. The transactions of the business in its head office at Delhi were mostly with sister concerns. These facts, according to the CIT (Appeals), showed that the business was not settled upon trust and cannot be said to be a business held under trust. The source for the business came from borrowings and contributions by the sister concerns and not from the trust, except to a meagre extent of ₹2,100/-. The property held under trust may no doubt include subsequent accretions to the corpus of the trust fund but it cannot include acquisitions in relation to which the trust stood in the capacity of a debtor to third parties, according to the CIT (Appeals). The business undertaking no doubt belonged to the assessee – trust and the business was also carried on by it, but for these reasons the business cannot be held to constitute property held under trust. Having held that the business was not held under trust, the CIT (Appeals) proceeded to consider the further question whether the carrying on of the *Katha* business was incidental to the attainment of the objects of the trust. It was submitted before him on the basis of clause 19 of the trust deed that the whole purpose of the business was to provide funds or generate income for being applied to the charitable activities listed in the trust deed. The submission was rejected by the CIT (Appeals) by holding that the fact that the income generated by the business was applied to the charitable purposes of the trust was not relevant and what was relevant was whether the business activity was itself incidental to the attainment of the objects of the trust, within the meaning of Section 11(4A) of the Act. According to the CIT (Appeals) the running of a *Katha* factory can hardly be said to be incidental to the attainment of the objects of the assessee – trust, which are the advancement of education, patriotism, Indian culture, etc. The fact that the whole or some part of the income of *Katha* business was to be applied in terms of the trust deed to the charitable objects would by itself

cannot render the carrying on the business as an activity incidental to the attainment of the objects of the trust.

10. It would appear that the assessee had taken up another objection before the CIT (Appeals) to the effect that the leasing out of the business unit to another entity did not amount to carrying on of a business activity. The CIT (Appeals) did not accept the contention, holding that where a business or commercial asset such as factory manufacturing *Katha* and *cutch* is leased to another entity for a monthly consideration termed as lease rental, the rental income would constitute business income in the hands of the lessor. According to the CIT (Appeals), leasing out of the factory is only one mode of exploiting a commercial asset for gain and such gain falls to be considered as profits and gains of business.

11. Certain other contentions regarding the computation of the business income were taken before the CIT (Appeals) as an alternative arguments and these have been dealt with by him, partly in favour of the assessee and partly against it. This part of the case need not detain us.

12. The assessee preferred a further appeal to the Tribunal in ITA No.3633/Del/96. The Tribunal, following its decision for the assessment year 1989-90 in ITA No.3641/Del/94 by order dated 30.09.1996, held that the *Katha* business carried on by the assessee was incidental to the attainment of the objects of the trust, which were for charitable purposes. As regards the position in law, after the amendment made to Section 11(4A) of the Act w. e. f. 01.04.1992, the assessee placed reliance on the judgment of the Supreme Court in *Assistant Commissioner of Income-tax v. Thanthi Trust*, (2001) 247 ITR 785 (SC) in which the effect of the amendment was considered. It was held that the Supreme Court has noted the amendment and held that it did not have any adverse effect on the claim of exemption under Section 11, provided the income from the business carried on by the trust is utilised by the trust for the purposes achieving the objects of the trust; that would be a case of the business activity being incidental to the attainment of the objects of the trust. The Tribunal held that this decision squarely

covered the controversy in the present case. In this view of the matter it directed the assessing officer to allow the exemption under Section 11 and thus allowed the appeal of the assessee.

13. It may be noted that the Tribunal did not specifically address itself to the question, which arose out of the order of the CIT (Appeals), whether the business itself can be said to be property held under trust within the meaning of Section 11(4) of the Act. There is no discussion in the order of the Tribunal as to the impact of the various clauses of the trust deed which were referred to by the CIT (Appeals) while making a distinction between the objects of the trust and the powers of the trustees.

14. In respect of all the other assessment years namely 1993-94, 1994-95, 2001-02 and 2005-06 to 2007-08, the Tribunal has followed the earlier order passed by it for the assessment year 1992-93 in ITA No.3633/Del/1996. There is no independent reasoning in any of them since the facts for all the years were the same as they existed in the previous year relevant to the assessment year 1992-93. In some of the orders, for instance the order of the Tribunal for the assessment year 2005-06, there is additional reference to the judgment of the Supreme Court in the case of *Thanthi Trust* (supra).

15. Section 11(1) of the Act grants exemption to the income derived from property held under trust wholly for charitable or religious purposes, to the extent to which such income is applied to such purposes in India. There is no exhaustive definition of the words "property held under trust" in the Act; however, sub-section (4) says that for the purposes of Section 11, the words "property held under trust" "includes a business undertaking so held". Sub-section (4A) as it stands amended by the Finance (No.2) Act, 1991 w. e. f. 01.04.1992 is in the following terms: -

> *"(4A) Sub-section (1) or sub-section (2) or sub-section (3) or sub-section (3A) shall not apply in relation to any income of a trust or an institution, being profits and gains of business, unless the business is incidental to the attainment of the objectives of the trust*

or, as the case may be, institution, and separate books of account are maintained by such trust or institution in respect of such business."

16. The question whether sub-section (4A) would apply even to a case where a business was held under trust was answered in the negative in several authoritative pronouncements starting from the judgment of the Lahore High Court in *Gadodia Swadeshi Stores v. Commissioner of Income Tax, Punjab*, (1944) 12 ITR 385. The general provision under Section 4(3)(i) of the 1922 Act exempted income derived from property held under trust from taxation. However, section 4(3)(ia) provided that any income derived from a business carried on on behalf of a religious or charitable trust would be entitled to exemption only if the business was carried on in the course of carrying out of a primary purpose of the trust or the work in connection with the business is mainly carried on by the beneficiaries of the trust. The contention of the revenue in that case was that since clause (ia) was a special provision dealing with the topic of exemption in respect of a business carried on for and on behalf of a trust, any claim for exemption as regards the profits of such business can be made only under that provision, and when the conditions laid down therein are not satisfied, it is not open to the assessee to fall back upon the general provision contained in Section 4(3)(i) and claim exemption thereunder on the ground that business is property. The Lahore High Court held that the fact that the business carried on on behalf of the trust failed to satisfy the two conditions laid down in Section 4(3)(ia) was no reason why it should not be exempted from taxation if it fell within Section 4(3)(i) and the main ground of the decision is that the two categories mentioned in the two clauses having been enacted as two different clauses, it must be taken that the one did not exclude the other. This judgment of the Lahore High Court was approvingly referred to by the Supreme Court in *J. K. Trust v. Commissioner of Income-tax*, (1957) 32 ITR 535. The judgment of the Supreme Court in *J.K. Trust v. CIT* (supra) was followed by the Supreme Court (a Bench of equal strength) in *Commissioner of Income-tax v. Krishna Warriar (P.)*, (1964) 53 ITR 176. By that time clause (ia) of Section 4(3)

had been enacted as a proviso to clause (i) of Section 4(3), by an amending Act of 1953. After referring to the judgment of the Lahore High Court (supra) and rejecting the argument of the revenue that a proviso in a statute be always read as limitation upon the effect of the main enactment Subbarao, J. (as he then was) observed as under: -

> "……*But it is not an inflexible rule of construction that a proviso in a statute should always be read as a limitation upon the effect of the main enactment. Generally the natural presumption is that but for the proviso the enacting part of the section would have included the subject-matter of the proviso; but the clear language of the substantive provision as well as the proviso may establish that the proviso is not a qualifying clause of the main provision, but is in itself a substantive provision. In the words of Maxwell, "the true principle is that the sound view of the enacting clause, the saving clause and the proviso taken and construed together is to prevail". So construed we find no difficulty, as we will indicate later in our judgment, in holding that the said clause (b) of the proviso deals with a case of business which is not vested in trust for religious or charitable purposes within the meaning of the substantive clause of section 4(3)(i).*"

17. Thus, if a property is held under trust, and such property is a business, the case would fall under Section 11(4) and not under Section 11(4A) of the Act. Section 11(4A) of the Act, would apply only to a case where the business is not held under trust.

18. In view of the above settled legal position, we are unable to accept the contention urged on behalf of the revenue before us that the provisions of Section 11(4A) are sweeping and would also take in a case of business held under trust.

19. The next question which we have to consider is whether, on the facts of the present case and having regard to the terms of the trust deed and the conduct of the trustees, it can be said that the *Katha* business was itself held under trust. There is a difference between a property or business held under trust and a business carried on by or on behalf of the trust. This distinction was recognised in *Addl.*

Commissioner of Income Tax, Gujarat v. Surat Art Silk, (1998) 121 ITR 1, a decision of five Judges of the Supreme Court. It was observed that if a business undertaking is held under trust for a charitable purpose, the income therefrom would be entitled to the exemption under Section 11(1) of the Act. In the case before us the finding of the CIT (Appeals), in his order for the assessment year 1992-93, is that the *Katha* business was not held under trust, but it was a business commenced by the trustees with the aid and assistance of borrowings from the sister concerns in which the settlors and the trustees or their close relatives had substantial interest, as well as from banks. It is thus with the help of the borrowed funds, or in other words, the funds not belonging to the assessee trust, that the *Katha* business was commenced and profits started to be earned. The CIT (Appeals) has also found that the earnings from the business were utilised to pay off the borrowings. It was for these reasons that he held that through the business undertaking belonged to the trust and the business was carried on by or on behalf of the trust, but for those reasons the business cannot be said to constitute "property held under trust". He made reference to clauses 19 and 20 of the trust deed in this behalf and noted that clause 19 provided that the trust may "carry on any business for or on behalf of or in the name of the trust for the sole object of supplying to income and profits thereof for the purposes and objects of the trust". Clause 20 provided that the trust may obtain financial help from banks, financial institutions, business houses and other organisations, etc. He was inclined to view these clauses only as powers enabling the trustees to commence and carry on business to augment the resources available to the trust. It was for these reasons that the CIT (Appeals) held that the *Katha* business was not held under trust. Unfortunately the Tribunal, which appears to have disposed of the appeal in a rather summary manner did not examine this aspect and merely endorsed the claim of the assessee. This is a matter of considerable importance and we would have thought that it was incumbent upon the Tribunal to have examined this fundamental aspect, for two reasons: firstly, under Section 11(4), it is only the business which is held under the trust that would enjoy exemption in respect of its

income under Section 11(1); secondly, there is a distinction between the objects of a trust and the powers given to the trustees to effectuate the purposes of the trust. The CIT (Appeals) also held for the assessment year 1992-93 that while the objects of the trust were certainly charitable, clauses 19 and 20 are mere powers conferred upon the trustees to carry on business, the profits from which would feed the charitable objects. There is no settlement of the business in *Katha* upon trust for the simple reason that the business itself was not in existence at the time of formation of the trust. The property held under trust was merely a sum of ₹2,100/-, contributed more or less equally by the settlors at the time of creation of trust on 08.09.1971. The business in *Katha* came into existence in the year 1972 and the production unit in Mahesh Udyog, Himachal Pradesh started production on 08.02.1973. Thus the *Katha* business was not even in the contemplation of the settlors and, therefore, could not have been settled upon trust.

20. A few decisions may be noticed which are of relevance to the point. In the case of *J. K. Trust v. CIT* (supra) one of the questions which arose was whether the office of managing agency which was an office of profit was in fact settled upon trust and, therefore, could be considered to be business held under trust. The Supreme Court held that for the purposes of Section 4(3)(i) of the 1922 Act, the office of managing agency was property which could be held under trust. The Revenue thereupon pointed out that on the terms of Exhibit 'A', which was the deed of trust executed by the settlors on 15.06.1945, the properties which the trustees are to hold and stand possessed of were only the sum of ₹1,00,000/- and any donations and contribution received by the trustees and all accretions thereto and investment in securities made from time to time representing the accretions, and contended that on the terms of the trust deed, the managing agency which was acquired on 10.09.1945 for a period of 20 years cannot be said to be property held under trust since no part of the initial amount of ₹1,00,000/-, which was settled upon the trust, was utilised in the acquisition of the managing agency so as to impress it with the character of accretion. While repelling this contention, the Supreme Court held as under, (T. L. Venkataraman Iyer speaking for the Court): -

> "……*But it is to be observed that clause (3) of the trust deed expressly provides for the acquisition of the business of managing agency on behalf of the trust and "with the help of the trust fund" and that precisely is what has happened and indeed, reading together Exhibits A and B, it is impossible to resist the conclusion that both the documents formed part of an integral scheme, and that what the settlors had in view in clause 3 of Exhibit A is the very managing agency, which was acquired under Exhibit B. There is considerable authority in England that when trustees carry on business with the aid of trust fund, the position in law is the same as if they actually employed it in the business, though, in fact, it be not actually invested therein.*"

Exhibit 'B' in the case of *J. K. Trust* (supra) was the document dated 10.09.1945 (memorandum of agreement) executed by the company constituting the trustees of the *J. K. Trust, Bombay* as its managing agent on the terms and conditions set out therein. It is important to notice that the trust deed, which is Exhibit 'A', provided *inter alia* that the trustees may, "with the help of the trust fund", for and on behalf of and for the benefit of the trust, carry on such business including the taking up and conducting of managing agency or selling agency of any company and may start such business and utilise the profits for all or any of the objects of the trust. Large powers were conferred on the trustees in the conduct of the business which included the power to raise and borrow money required for the purpose of trust. It may be seen that under the trust deed in the case of *J. K. Trust* (supra) the trustees were authorised to carry on business "with the help of the trust fund". It has also been noticed by the Supreme Court that the sum of ₹1,00,000/- was given as security by the trustees under Exhibit 'B' for the due performance of their obligations as managing agents. It was in the background of these facts that the Supreme Court held that the managing agency business, which was acquired with the help of the trust fund, could be considered as business held under trust and that the fact that the amount of ₹1,00,000/- which was settled upon trust was not utilised for the acquisition of the business, but was given merely as security deposit for the due performance of the duties of the managing agents, did not matter. The Court was, in the light of these facts and circumstances, inclined to hold that both

the documents, namely Exhibits 'A' and 'B', formed part of an integral scheme and what the settlors had in view in clause 3 of Exhibit 'A' was the very managing agency which was acquired under Exhibit 'B'. The test appears to us to be that the business, if it is to be considered as property held under trust, should have been either acquired with the help of the fund originally settled upon trust or the original fund that was settled upon trust must have a substantial and real connection with the later acquisition or carrying on of the business by the trustees. The facts of the present case do not measure up to the test. The fund originally settled upon trust was a meagre amount of ₹2,100/- at the time of the creation of the trust on 08.09.1971. It is undisputed that the *Katha* unit in Himachal Pradesh was set up in the year 1972 with the aid and assistance of the borrowed amounts, the borrowings being both from the concerns in which the settlors/ trustees held substantial interest and from commercial banks. There is thus no nexus or integration between the amount originally settled upon trust and the later setting up and conduct of the *Katha* business. Moreover, the distinction between the original trust fund and the later commencement of the business with the help of the borrowed funds should be kept in mind in the context of ascertaining whether the particular *Katha* business was even in the contemplation of the settlors of the trust. It is difficult to view the original settlement of ₹2,100/- upon trust and the setting up of the *Katha* business as part of an integrated scheme even apart from the fact that the business was not acquired or carried on with the help of the original trust fund.

21. In *Thiagesar Dharma Vanikam v. Commissioner of Income-tax*, (1963) 50 ITR 798 a Division Bench of the Madras High Court held that a business carried on behalf of a trust "*rather indicates a business which is not held in trust, than a business of the trust run by the trustees*". In that case the business was carried on by the trustees for and on behalf of the trust and it was found as a fact that that business was itself held under trust. In *Raja P. .C. Lall Choudhary Vs. Commissioner of Income Tax, Bihar & Orissa* (1957) 31 ITR 226, the Patna High Court ruled that Section 4(3)(i) of the Indian Income Tax Act, 1922, which corresponds to Section 11(1) of the 1961 Act, confers an exemption from tax only

where the property itself is held under a trust or other legal obligation; it does not apply to cases where a trust or legal obligation is not created on any property, but only the income derived from any particular property or source is set apart and charged for a charitable or religious purpose. In *Commissioner of Income Tax. v. P.K. Barooah, Vice-President, Jorhat Races* (1970) 77 ITR 967, the Assam and Nagaland High Court, referring to the judgment of the Patna High Court (supra) held that the surplus fund of a trust, which was claimed to be exempt on the footing that it was property held under trust within the meaning of Section 11(1) of the Act, was not property held under trust since the property from which the surplus was generated was itself not held under trust. Observing that the expression "legal obligation" cannot be separated from the word "property" appearing in Section 11(1), the Court expressed itself as under :

> *"The expression "legal obligation" cannot be separated from the "property" itself which in the instant case is a horse-racing concern, inasmuch as law enjoins that such property must be held under a trust or other legal obligation and not the fund derived therefrom. We have already shown that Jorhat Races were not the subject-matter of a trust and only a trust has been created in respect of the surplus fund. The surplus fund really emanates from a property which is not a subject-matter of the trust and as such in the absence of any legal obligation fastened thereto, no exemption can be allowed under Section 11 of the Act."*

These cases reiterate the position that the question to be examined is whether the business itself is held under trust or is merely carried on by and on behalf of the trust. It is also significant that Section 11(1) of the Act starts with the expression "subject to the provisions of Sections 60 to 63.....". These Sections find place in Chapter V of the Act. Section 60 provides for the consequences of a transfer of income where there is no transfer of assets. It says that where a person transfers merely the income from an asset without transferring the asset itself, he would continue to be chargeable to income tax. Section 61 provides for the consequences of a revocable transfer of assets and says that the same would be the position where a person is in receipt of income by virtue of a revocable transfer of assets. Section

62 provides for the consequences of a transfer of assets for specified period. It is an exception to Section 61. Generally a person has to get rid of the asset itself before ceasing to be assessable in respect of the income from that asset. A mere direction that the income from the business shall be applied to the charitable objects of a trust, without there being a settlement of the business itself upon trust, does not result in any trust or legal obligation.

22. We now proceed to consider the question whether the carrying on of the business in *Katha* was incidental to the attainment of the objects of the trust. We fail to see any connection between the carrying on of the *Katha* business and the attainment of the objects of the trust, which are basically for the advancement of education, inculcation of patriotism, Indian culture, running of dispensaries hospitals, etc. The mere fact that whole or some part of the income from *Katha* business is ear-marked for application to the charitable objects would not render the business itself being considered as incidental to the attainment of the objects. We are in agreement with the view taken by the CIT (Appeals) in his order for the assessment year 1992-93 that the application of the income generated by the business is not the relevant consideration and what is relevant is whether the activity is so inextricably connected or linked with the objects of the trust that it could be considered as incidental to those objectives. The examples, appositely given by the CIT (Appeals) in his order, clarify the position: the instance of a charitable trust established for providing medical relief running a nursing home in the process, or a trust for advancement of education running a publishing house or a newspaper.

23. It was contended on behalf of the assessee that the mere letting out of the factory on lease w. e. f. 01.01.1992 does not amount to carrying on of any business. We are unable to accept this contention. Initially the assessee carried on the business itself. The production unit was set up in 1972 and started production on 08.02.1973. For a period of five years the assessee was itself carrying on business. In the year 1978 it was given on lease to M/s. Shankar Trading Co. (P)

Ltd., a sister concern in which the close relatives of the trustees had substantial interest. The lease rent which was initially ₹25,000/- per month was revised to ₹50,000/- per month w. e. f. 01.04.1987 and thereafter to ₹1,00,000/- per month w.e.f. 31.12.1991. There is ample authority for the proposition that leasing out of a factory for monthly rentals is one form of carrying on a business. The judgment of the Calcutta High Court in *Directors of Income Tax (Exemption) v. Sahu Jain Trust*, (2011) 243 CTR (Cal.) 131 dealt with a different factual situation. There the trust derived income from sub-letting tenanted properties. This activity was branded as business activity and the provisions of Section 11(4A) of the Act were invoked. The Calcutta High Court held that there was no material on record to justify the view taken by the assessing officer that it was a business activity; it was just a simple sub-letting not amount to carrying on of any business. The present case does not fall under the category dealt with by the Calcutta High Court. We are, therefore, not inclined to accept the submission that no business was carried on by the trustees.

24. Reference was then made on behalf of the assessee to the judgment of the Supreme Court in *Thanthi Trust* (supra) and it was contended that if the profits of the business carried on by the trust are utilised by the trust for the purposes of achieving the objectives of the trust, then the business should be considered to be incidental to the attainment of the objects of the trust. The exact observations of the Supreme Court are as under: -

> *"As it stands, all that it requires for the business income of a trust or institution to be exempt is that the business should be incidental to the attainment of objectives of the trust or institution. A business whose income is utilised by the trust or the institution for the purposes of achieving the objectives of the trust. In any event, if there be any ambiguity in the language employed, the provision must be construed in a manner that benefits the assessee."*

Prima facie the above observations would appear to support the assessee's case in the sense that even if the *Katha* business is held not to constitute a business held under trust, but only as a business carried on by or on behalf of the trust, so long as

the profits generated by it are applied for the charitable objects of the trust, the condition imposed under Section 11(4A) of the Act should be held to be satisfied, entitling the trust to the tax exemption.

25. In our opinion these observations have to be understood in the light of the facts before the Supreme Court. Thanthi Trust carried on the business of a newspaper and that business itself was held under trust. The charitable object of the trust was the imparting of education which falls under Section 2(15) of the Act. The newspaper business was certainly incidental to the attainment of the object of the trust, namely that of imparting education. The observations were thus made having regard to the fact that the profits of the newspaper business were utilised by the trust for achieving the object, namely education. The type of nexus or connection which existed between the imparting of education and the carrying on of the business of a newspaper does not exist in the present case. There is no such nexus between the *Katha* business and the objects of the assessee – trust that can constitute the carrying on of the *Katha* business an activity incidental to the attainment of the objects, namely advancing of education, patriotism, Indian culture, running of hospitals and dispensaries, etc. It would in our opinion be disastrous to extend the sweep of the observations made by the Supreme Court (quoted above) in the case of *Thanthi Trust* (supra), on the facts of that case, to all cases where the trust carries on business which is not held under trust and whose income is utilised to feed the charitable objects of the trust. We are, therefore, of the respectful opinion that the observations of the Supreme Court must be understood and appreciated in the background of the facts in that case and should not be extended indiscriminately to all cases.

26. It was contended on behalf of the assessee that in case we hold that the assessee-trust is not eligible for exemption because the *Katha* business was itself not held under trust, it would produce an anomalous or discriminatory result inasmuch as all that is required is for the settler of the trust to declare that the *Katha* business itself would be held in trust. It is not for us to comment on the

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contention; we cannot question the legislative wisdom and if there is really an anomalous or discriminatory resultant position, it is for the legislature to take care of it. It is not for us to enter "such a complex arena in which no perfect alternatives exist" as observed by Justice Stewart of the Supreme Court of the USA in *Sam Antonio School District Vs. Rodrigous* (1973) 411 US 1.

27. For the reasons given above we answer the substantial questions of law in all the appeals against the assessee and in favour of the Revenue. The appeals of the Revenue are accordingly allowed with no order as to costs.

(R.V. EASWAR)
JUDGE

(S. RAVINDRA BHAT)
JUDGE

NOVEMBER 20, 2012
hs/vld